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WASHINGTON, D.C.

September 10, 2007

Mary L. Cottrell, Secretary Massachusetts Department of Public Utilities One South Station, 2nd Floor Boston, MA 02110

RE: Investigation by the Department of Public Utilities on its own Motion into Rate Structures that will Promote Efficient Deployment of Demand Resources - D.P.U. 07-50

Dear Ms. Cottrell:

Enclosed for filing on behalf of Associated Industries of Massachusetts please find their comments on the above captioned matter.

Please contact me if you have any questions regarding the attached.

Regards,

Robert A. Rio, Esq.

Robert A Ros

Senior Vice President – Government Affairs Associated Industries of Massachusetts

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COMMONWEALTH OF MASSACHUSETTS DEPARTMENT OF PUBLIC UTILITIES

Investigation by the Department of Public Utilities)	D.P.U. 07-50
on its own Motion into Rate Structures that will)	
Promote Efficient Deployment of Demand Resources)	

COMMENTS OF ASSOCIATED INDUSTRIES OF MASSACHUSETTS

I. INTRODUCTION

Associated Industries of Massachusetts (A.I.M.) submits the following comments in response to the Department of Public Utility's request for comments on June 22, 2007 in the above captioned docket.

Associated Industries of Massachusetts is the largest employer association in Massachusetts. A.I.M.'s mission is to promote the well-being of its more than 7,000 members and their 680,000 employees and the prosperity of the Commonwealth of Massachusetts by improving the economic climate, proactively advocating fair and equitable public policy, and providing relevant, reliable information and excellent services. A.I.M. members include large and small employers from the industrial, commercial and service sectors, all of whom would be impacted by this proposal.

The Department issued an Order opening an Investigation into Rate Structures that will Promote Efficient Deployment of Demand Resources requesting comments about the issue generally and about a strawman proposal specifically. For the reasons stated more fully below, Associated Industries of Massachusetts does not believe that Revenue Decoupling is needed or desirable.

II. EXECUTIVE SUMMARY

Massachusetts has the highest cost of electricity in the continental United States, striking at the heart of our economy. Medium and large commercial and industrial companies constantly cite the price of electricity as an impediment to expanding or staying in Massachusetts. In an A.I.M. energy survey, 95% of respondents said electricity costs are a problem; almost 80% said costs had forced them to cut back on employee salaries and benefits, lowered their profit margin or forced them to stop making certain product lines in Massachusetts; and about half believe that high electricity costs will drive future investment and location decisions in Massachusetts. C&I customers, unlike homeowners, are extremely sensitive to marginal increases in electricity costs.

A.I.M. believes that the proposed radical change in rate structure fails any value test for electricity consumers. It will actually discourage energy efficiency and demand response by weakening the price signals to consumers that have driven change, and making paybacks on efficiency investments less attractive. It distracts the DPU from the real rate design reform and individual rate cases that are the most valuable way the Department can advance conservation and efficiency and moderate or reduce high electricity costs.

We doubt, in fact, that the "problem" of utilities' incentives with regard to conservation is a real one. Rather than focusing on whether utilities are losing money because of energy efficiency, the DPU should investigate whether the utilities and consultants are benefiting too much under current energy efficiency incentives and not returning those savings adequately to customers.

III. COMMENTS

A.I.M. appreciates the opportunity to provide comments regarding the above referenced docket.

A.I.M.'s participation before the DPU and in other energy related forums starts with the observation that our state regrettably has the highest cost of electricity in the continental United States. This cost strikes at the heart of our economy affecting households and businesses, and severely affecting job retention and growth.

Some recent examples of how our high cost of electricity and other costs are impacting long time Massachusetts employers include:

- In March, Revere Copper Products, a company started by Paul Revere in 1801
 (and whose copper was used on the dome of the Massachusetts State House in 1802) announced that their New Bedford facility would close and cited electricity rates as the principal culprit, putting 85 people out of work.
- Also that week, Fox River Paper Products announced the closing of their Great
 Barrington mill which had been in operation since 1900. The press release noted
 "rising production costs" as one of the reasons for closing the mill, which resulted
 in 137 jobs lost.
- In July, Quaker Fabrics in Fall River, founded in 1941 shut their doors putting 900 workers out of work.
- MeadWestvaco, specifically citing electricity costs, announced in August they were closing their South Lee plant, resulting in job losses of 70 workers.

A.I.M. members, specifically those in the medium and large commercial and industrial sector, constantly cite the price of electricity as one of the impediments to expanding or staying in Massachusetts, and data shows that the large commercial and industrial load is declining in most utility territories. Preliminary results from our recent energy survey indicated that almost 50% of the respondents believe that high electricity costs will drive future investment decisions in Massachusetts or will determine the future of existing operations here. Only 5% indicated electricity costs are not a problem.

Unlike homeowners, whose sensitivity to marginal increases in electricity costs is not high, C&I customers are extremely sensitive even to small increases on the order of a quarter cent per kWh, as this increase could mean hundreds of thousands of dollars in additional cost and completely wipe out expected profit for the year. Almost 80% of our survey respondents indicated that higher electricity rates have cut their profit margin and forced them to cut back on employee salaries and benefits or in fact forced them to stop making certain products in Massachusetts.

With this as background, we believe that the radical change in rate structure envisioned in this investigation fails any value test for electricity consumers – households as well as businesses. Massachusetts needs to seize every opportunity to reduce electricity costs. However, we question whether this proposal at this time accomplishes such a goal. First, it fails to promote energy efficiency and demand response – in fact it discourages such actions because a portion of the consumer savings are transferred to utilities in the form of higher rates, making paybacks on efficiency investments less attractive. Most importantly, however, it distracts the Department from the real rate design reform and individual rate cases – which are the most valuable way the DPU can

advance conservation, efficiency and moderate or reduce high electricity costs. In our survey, almost 50% of respondents indicated that while conservation has reduced their overall use of electricity, their total cost of electricity has actually risen.

In this proceeding, the DPU states:

"The inherent conflict between the incentives to increase sales promoted by current revenue collecting mechanisms and the reduced consumption resulting from the use of demand resources creates a significant barrier to the efficient deployment of these resources."

It is not clear to A.I.M. what evidence supports this statement. A.I.M. has serious doubts that it is in fact true. The fact that the D.P.U., not the utilities, initiated this proposal is further reason that this investigation may be several years too early. Prior to continuing the decoupling discussions DPU needs to investigate whether or not the basic premise of this order is valid. Therefore the first level of inquiry is whether the problem the Department seeks to address is a problem at all.

We do not see any severe conflicts within the utilities between reduced consumption and reduced revenue. Demand reductions come in many forms, not all of which are initiated by the utility. Some are passive in regard to the deliverer of electricity, as when customers buy new and more efficient appliances or other equipment over the course of normal appliance turnover and outside of utility run programs. Other efficiency is more active, as when the utility or third party provider is involved in rebates or other funding mechanisms as part of their Demand Side Management (DSM) program. Some of this is offset, of course, by more economic growth and the purchase of more equipment that uses electricity, especially on the residential side.

In addition to the millions of dollars spent by utilities under their DSM program and the millions of dollars spent by consumers on direct energy conservation efforts that are not counted in the DSM program, there are numerous organizations that encourage on-site renewable power as well as private and non-profit companies that work on demand response and other proactive programs. In fact, many of the newer, more efficient programs are using market driven third party participants to coordinate the energy savings, a much more preferable option and not necessarily counted under the utilities DSM programs. Because of all this activity, A.I.M. sees no evidence that revenue side utility conflicts are in any way inhibiting the growth of demand response or energy efficiency programs in the private sector.

Nor do we see any evidence that the amount of money spent on demand response would be significantly higher with additional cooperation of the utility. People are reducing their use to save money from some of the highest electric rates in the country and for economic survival. Like any other investment, if the payback is appropriate it will likely be done. Whether the utility is part of the mix is irrelevant for commercial and industrial consumers. Allowing utilities to take a piece of the savings will discourage conservation and makes valid conservation efforts more difficult to justify, whether funded by utility programs or private funds.

In the final analysis, we question the validity of raising revenue decoupling at all. It suggests that while households and businesses deal with high energy costs (and more costs will be part of society's response to climate change) decoupling essentially insulates utilities from sharing in the solutions to these problems. Moreover, the fundamental question is why should a utility be insulated from both the up side or down side of

competition – in so far as energy conservation is competition to energy supply – when every other business is not.

The order also contains the following statement:

Once charges are set, electric and gas companies have a strong incentive to take actions to increase sales (thereby increasing revenue) and an equally strong incentive to avoid any decreases in sales (thereby decreasing revenue).

One again, A.I.M. does not believe this statement to be accurate. In fact, the current energy efficiency program is very rewarding for utilities.

A.I.M. is a staunch supporter of energy efficiency of all types. We have partnered with utilities and state agencies and colleges and universities to offer broad educational seminars on efficiency. However, the return must be quantifiable and the savings must return to the ratepayers. As stated above, the cost of electricity is rising for many despite a reduction in the use of electricity. While this is not necessarily the fault of the utilities, this outcome discourages participation in efficiency programs and leads to shutdowns and other unintended consequences mentioned above.

According to the Division of Energy Resources (DOER)¹ a total of 8% (or \$28 million over the three-year study period) goes to "Shareholder Incentive" (incentives awarded to utilities for meeting or exceeding their energy efficiency goals). This is in addition to administrative costs charged by utilities and others.

The same DOER report also indicates there are significant savings to the utilities as a result of reduced need for future infrastructure, such as poles and transmission lines. The savings, as quantified by DOER, total approximately \$325 million over the same

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¹ DOER – A Summary of the Performance of Electric Energy Efficiency Programs funded by Ratepayers between 2003 – 2005, April 2, 2007, page 10.

time period, which is more than the dollar amount of customer incentives during the same period (approximately \$220 million). If the "Shareholder Incentives" are added to the stated savings the utilities receive in the reduction in fixed costs, the total incentives to utilities is *over 350 million dollars* on what is only a 375 million dollar program.

Therefore, for every dollar collected from ratepayers, the utilities, according to DOER, save or are rewarded an equal amount. While some of this may be classified as avoided cost, this is still a very good return. Clearly, the utilities are compensated adequately under the current energy efficiency programs.

Of course, the infrastructure savings described above are in the context of the current DSM revenues. Should other passive energy efficiency occur, the utilities will also benefit on a dollar for dollar amount, without any active participation. This is a disquieting result that certainly undercuts the notion that the utilities need guaranteed revenue as they are losing money because consumers are getting smart about energy conservation and demand response.

Utility run DSM programs have been around for many years. While it may have made sense in the past for utilities to run DSM programs, it makes little sense now, especially for the C&I customer. The very fact that decoupling is the subject of a DPU investigation is exactly the reason the utilities should not be main players in the energy efficiency market. It may be time to extricate the utilities from DSM programs and rely on market-based incentives outside of the DSM program, particularly in regard to large commercial and industrial consumers.

Ignoring the financial return that utilities already receive from the program, the DOER has estimated that the current demand response programs result in only

approximately a 0.7 percent reduction in demand, although electricity use is still increasing at historic growth rates due to additional consumption. We do not believe this is a particularly significant reduction in revenue. Even if this were to be doubled over the next few years (an aggressive goal considering typical annual growth), we still believe the remaining revenue stream from consumers provides sufficient revenue for utilities. Decoupling subsidies are simply unnecessary. Every other organization A.I.M. is familiar with would either absorb such an impact or engage in management driven responses to ameliorate any financial impact.

A.I.M. certainly appreciates that there are fixed costs to run a utility that are not always comparable to the amount of electricity provided. Utilities may even see per capita revenue declines because of future energy efficiency. However, utilities need to understand new economic realities. Energy efficiency, unlike unplanned weather changes, result in permanent changes in the per capita amount of electricity being used and the utility should make permanent changes in their operations to address this. They are not unique in operating in a world where less of a product is used and utilities need to begin realigning and managing their operations in the face of such permanent changes to their business. This may involve difficult societal discussions and issues that will require a fundamental change in the way they are operated. But it should not result in a governmental mandate for guaranteed revenue regardless of the real underlying costs and management of the system. It is not the responsibility of consumers to make sure the utilities remain revenue neutral - it is only the responsibility of the consumer and the DPU to make sure the utilities collect enough money to run a reliable system and have the opportunity for a fair rate of return, not a fully guaranteed revenue stream.

While we recognize that organizational changes take time and rightfully should be implemented deliberately, the difficult question going forward is for the DPU to determine legitimate costs and appropriate return, and how those costs are billed to consumers. Since many of the utilities have not had full rate cases before the DPU for many years, it is extremely difficult to predict what these costs should be. Without benefit of a detailed and exhaustive rate case and cost allocation, it is impossible to adequately support any revenue enhancements for the utilities. In fact, the starting point for the Department should be a comprehensive and open stakeholder process to create a rate design template for all future rate cases.

Under any scenario, the DPU must be convinced that the utilities have done everything, both short and long-term, to reduce their costs commensurate with system reliability. This includes organizational changes and technology improvements, mergers, and management of personnel and benefits to minimize costs and maximize efficiencies. Utilities need to be required to identify and justify every penny spent as just and reasonable and show what they are doing to reduce costs to ratepayers. Like every other company, they are not in any way precluded on their own from instituting cost saving measures to maximize profit and make up for declining sales.

Rather than focusing on whether utilities are losing money because of energy efficiency, the DPU should investigate whether the utilities and consultants are benefiting too much under current energy efficiency incentives and not returning those savings adequately to customers. Every household and business, including utilities, need to be partners in the societal goal of reducing energy - given the existing programs that may mean sharing savings more than they have in the past.

Because of the varying load and the sensitivity to price, the ramifications of decoupling for C&I customers will be very different than for residential customers, where usage patterns and energy efficiency gains are much more homogenous and this alone should slow down discussions about decoupling since the downside of getting it wrong is an exodus of more C&I customers. Also, any discussion about decoupling should begin with the absolute stipulation that all current programs and guarantees currently afforded utilities are sunsetted. This includes shareholder incentives from the current energy efficiency program, and a fundamental discussion concerning the way that return on equity is calculated for utilities since risk is reduced under decoupling. Allowing both sources of revenue to continue is unnecessary in terms of both rate setting and energy efficiency.

Finally, there are currently numerous legislative proposals pending as well as regulatory proposals that are being debated and likely to be acted upon soon. These include substituting current energy efficiency programs with other more flexible programs as well as proposals to realign and reinvigorate the current demand response and energy efficiency programs. Decoupling is only one piece of the puzzle. There needs to be coordination of all these proposals since one agency or branch's decisions could clearly conflict or negate the actions of the other.

Rather than pursuing the course proposed by DPU 07-50 we urge the DPU to instead focus its resources on rate design and the ordering of individual rate cases.

IV. REQUEST TO APPEAR AS PART OF A PANEL

A.I.M. would like to be part of a panel commenting as part of this proposal.

A.I.M. represents over 7,000 businesses in Massachusetts, including many medium and large C&I customers. Our comments as part of the panel will detail and expand upon our comments above. The contact information is:

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Should you have any questions please do not hesitate to contact me at 617-262-1180.

Respectfully submitted,

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